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IN THE

Supreme Court of the United States

OCTOBER TERM, 1955.

No. 520

JULIAN LENTIN,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit, entered in the above entitled case on October 14, 1955.

CITATIONS TO OPINION BELOW.

The judgment of the United States District Court for the Northern District of Illinois, Eastern Division (hereinafter referred to as the "District Court"), in a civil proceeding captioned *Chester A. Bowles, Administrator, Office of Price Administration* vs. *Julian Lentin d.b.a. J. Lentin Lumber Company,* Civil Action No. 44C 476, is unreported. This Judgment was affirmed on appeal in *Bowles* v. *Lentin,* 151 F. 2d 615 (C.A. 7), cert. denied,

327 U.S. 805, rehearing denied 328 U.S. 877. The opinion of the Tax Court of the United States is reported at 23 T.C. # 16 (1954) and is printed in the Transcript of Record, p. 24. The opinion of the United States Court of Appeals printed in Appendix B hereto at p. 3a, *infra*, is unreported.

JURISDICTION.

The judgment of the United States Court of Appeals was entered on October 14, 1955. The jurisdiction of this court is invoked under 28 U.S.C., Section 1254 (1).

QUESTIONS PRESENTED.

1. Whether the doctrine of collateral estoppel is available to the Tax Court where the deduction of a fine, penalty or forfeiture is claimed.

2. Whether collateral estoppel bars relitigation of an issue in the second suit based upon a failure to prove the contrary of the fact in the first suit.

STATUTES INVOLVED.

The statutes involved are the Emergency Price Control Act of 1942, as amended, 56 Stat. 23, 50 U.S.C.A. App. Section 925(e), printed in Appendix A, *infra*, p. 1a and Section 23(a) (1) (A), Internal Revenue Code, 1939, printed in Appendix A, *infra*, p. 2a.

STATEMENT.

Petitioner was adjudicated a willful violator of the Emergency Price Control Act of 1942, as amended, and judgment was entered against him for twice the amount of the overcharge. *Bowles, Administrator, Office of Price Administration* vs. *Julian Lentin, d.b.a. J. Lentin Lumber Company, Civil Action* No. 44C 476; aff'd *Bowles* v.

Lentin, 151 F. 2d 615 (C.A. 7, 1945), cert. denied 327 U.S. 805 (1941), reh. denied 328 U.S. 877. Petitioner paid the amount claimed herein as a deduction to the Government in satisfaction of the judgment, which deduction was disallowed by the Commissioner of Internal Revenue and a deficiency of $16,676.34 assessed for the year 1946. A petition for redetermination of the deficiency was filed in the Tax Court of the United States. The petitioner requested the court, in effect, to re-examine the issue of wilfullness in the tax proceeding and contended that the claimed deduction would not frustrate public policy (R. 4). The Commissioner answered, alleging the petitioner was collaterally estopped from placing in issue the fact of wilfullness (R. 13). Petitioner's repeated motions to strike this defense were unsuccessful (R. 15, 17). No hearing on the merits was, therefore, attempted or obtained. The Tax Court held the determination of the District Court that petitioner's violation of the Emergency Price Control Act was "wilful" collaterally estopped petitioner from relitigating this issue in the tax proceeding. The Tax Court, having determined what it deemed to be the sole issue before that court by the use of the doctrine of collateral estoppel, automatically disallowed the claimed deduction stating that to allow the same would frustrate clearly defined public policy, citing *Jerry Rossman Corporation* v. *Commissioner,* 175 F. 2d 711 (C.A. 2, 1949). The jurisdiction of the United States Court of Appeals, Seventh Circuit, was invoked by petition to review the decision of the Tax Court pursuant to Rule 27 of the Rules of the United States Court of Appeals. The court below affirmed the judgment of the Tax Court.

REASONS FOR GRANTING THE WRIT.

The Tax Court of the United States has utilized the tax law as a sanction to enforce other regulatory legislation. Thus, ordinary and necessary business expenses under Section 23(a) (1) (A), I.R.C., 1939, though otherwise qualifying will be disallowed if in contravention of the supervening judicial gloss of public policy. A penalty paid to the Government for violation of regulatory legislation had been deemed *per se* in contravention of public policy and therefore non-deductible until this Court's decision in *Commissioner* v. *Heininger,* 320 U.S. 467 (1943). Prior thereto, it was sufficient for the Tax Court to determine the fact of violation as decisive of the issue of deductibility, but the *Heininger* case abandoned the theory that payment of sums arising out of an illegal transaction were *per se* non-deductible. The case of *Jerry Rossman Corporation* v. *Commissioner,* 175 F. 2d 711 (C.A. 2, 1949) analyzed the effect of *Commissioner* v. *Heininger,* on the issue of the relation between the tax laws and their use as sanctions in the scheme of enforcement of unrelated regulatory legislation. The opinion of Judge Learned Hand in the *Rossman* case gives content to the term "public policy" and indicates that the payment of a fine, penalty or forfeiture will be allowed or disallowed entirely dependent on how the court obligated to make that decision in each instance views deductibility in terms of weakening or strengthening regulatory legislation: in effect, will the refusal to allow the claimed deduction act as a deterrent to potential violators, or will allowance thereof make others less solicitous of compliance. Thus, that a fine, penalty or forfeiture has been assessed against the taxpayer in a proceeding involving legislation other than the tax law is of itself no longer determinative of the deduction thereof. As to deduction of such expenditures, Judge Hand said:

> "Each may 'frustrate the sharply defined policies' of a statute; that will depend upon how one views their deterrent effect. We hold therefore that in every case the question must be decided *ad hoc.*"

The clear implication of *Rossman* was to impose upon the Tax Court an independent duty of determining the future enforcement effect of allowability or nondeduction in every situation involving a fine, penalty or forfeiture arising by reason of the violation of regulatory legislation. Thus, notwithstanding the character of that violation, the Tax Court cannot rely upon a judicial determination of guilt, nor of a certain character of guilt so determined, as decisive of the issue before that court: whether non-allowance of the claimed deduction will result in strengthening the underlying legislation or have no effect at all. The use of the doctrine of collateral estoppel in any such situation by the Tax Court, however, results in abandonment of this lesiglatively directed and judicially defined duty. An illustration is the present case. The petitioner was determined to be a "willful" violator of regulatory legislation and paid a penalty to the Government. The Tax Court relied upon this finding in the prior proceeding without independent examination into the circumstances surrounding the issue and thus automatically disallowed the claimed deduction. The finding of the District Court in the *O.P.A.* case became a mandate of non-allowance and, in effect, was determinative of the independent value judgment actually required of the Tax Court. Use of the doctrine of collateral estoppel resulted in the abdication by the Tax Court of its duty to decide the effect on potential violators in the same circumstances as the taxpayer. Further, the regulatory legislation may contain definitions peculiar to its own purpose, whereupon sanctions available by use of the tax

laws have no relevancy to the circumstances encompassed by such definitions. Thus, under the legislation in question an advertent act lacking malice and founded upon an unsupportable but honestly conceived proposition of law was denominated a willful act. *R.F.C.* v. *Foust Distilling Co.*, 103 Fed. Supp. 167 (D.C., Pa., 1952). Clearly, the additional sanction imposed against a "willful" violator in this circumstance could not deter further erroneous but honest reliance. The determination of "wilfulness" of itself, could not then control the issue in the Tax Court involving the claimed deduction of a fine, penalty or forfeiture, since automatic disallowance may not deter future violators in the same circumstances. There is thus seen to be no necessary controlling correlation between a prior judicial determination of guilt involving other regulatory legislation and the issue which the Tax Court itself must determine. The *Heininger* case stated that each case should depend upon its peculiar circumstances, and the *Rossman* case stated that this decision was *ad hoc*. Judge Hand stated in the latter case that this determination is necessarily made with a view to the basic philosophy underlying the criminal law. Finally, if the Tax Court were to utilize the findings of fact in prior judicial decisions, whether mediate or ultimate data in that decision, as controlling the ultimate issue before the Tax Court, the loser's risk in the first suit becomes enlarged beyond all rational bounds. The doctrine of collateral estoppel, utilized in any tax case where previous thereto a business enterprise was fined or penalized, would create a situation where the prior decision would control an ultimate issue unrelated in any sense to the first decision. To preclude this effect, the rationale in the case of *The Evergreens* v. *Nunan*, 141 F. 2d 927 (C.A. 2, 1944) is stated:

"• • • no fact decided in the first whether 'ultimate' or a *'mediate datum,'* conclusively establishes any *'mediate datum,'* in the second, or anything except a fact 'ultimate' in that suit." (p. 931)

The Government here argued that to permit the allowance would result in mitigating the penalty assessed. This would preclude the deduction of *any* penalty, notwithstanding the clear rationale in opposition to this suggestion found in *Jerry Rossman Corporation* v. *Commissioner*. By the use of the doctrine of collateral estoppel the Tax Court and Court of Appeals came to the same conclusion suggested by the Government. It was never intended that the Tax Court be permitted to abandon its duty of independent administration of this area of the tax law by the use of this legal doctrine.

2. Of less national concern, but important to the proper application of the doctrine of collateral estoppel, was the failure of the Tax Court to perceive its inapplicability here. The Emergency Price Control Act of 1942, as amended, 56 Stat. 23, 50 U.S.C.A. App. Section 925(e), placed the burden of disproving a willful violation of the Act on the defendant therein. This presumption of wilfullness could be overcome only by a sufficiency of proof offered by the defendant. In the event he failed to make a showing deemed sufficient to overcome the presumption, an affirmative finding of willfullness resulted. Thus, the finding of wilfullness under the Act results from an absence rather than presence of proof. It is not conceived by the petitioner here that any case has so far extended the doctrine of collateral estoppel as to bar relitigation of a "fact" found in a prior adjudication resulting from an absence of proof.

CONCLUSION.

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A.

Emergency Price Control Act of 1942, as amended, 56 Stat. 23, 50 U.S.C.A. App. Section 925(e):

"If any person selling a commodity violates a regulation, order, or price schedule prescribing a maximum price or maximum prices, the person who buys such commodity for use or consumption other than in the course of trade or business may, within one year from the date of the ocurrence of the violation, except as hereinafter provided, bring an action against the seller on account of the overcharge. In such action, the seller shall be liable for reasonable attorney's fees and costs as determined by the court, plus whichever of the following sums is the greater; (1) Such amount not more than three times the amount of the overcharge, or the overcharges, upon which the action is based as the court in its discretion may determine, or (2) an amount not less than $25 nor more than $50, as the court in its discretion may determine: Provided, however, That such amount shall be the amount of the overcharge or overcharges or $25, whichever is greater, if the defendant proves that the violation of the regulation, order, or price schedule in question was neither wilfull nor the result of failure to take practicable precautions against the occurrence of the violation. * * * If any person selling a commodity violates a regulation, order, or price schedule prescribing a maximum price or maximum prices, and the buyer either fails to institute an action under this subsection within thirty days from the date of the occurrence of the violation or is not entitled for any reason to bring the action, the Administrator may institute such action on behalf of the United States within such one-year period."

Following is Section 23(a) (1) (A) Internal Revenue Code of 1939, 26 U.S.C. 1952 ed., Section 23:

"Internal Revenue Code of 1939:

Sec. 23. Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

(a) *Expenses.*—

(1) [As amended by Section 121(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798]

Trade or business expenses.—

(A) *In General.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *."

APPENDIX B.

Opinion of the United States Court of Appeals for the Seventh Circuit.

No. 11401. OCTOBER TERM AND SESSION, 1955.

JULIAN LENTIN,
vs.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Petition for Review of a Decision of the Tax Court of the United States.

Before DUFFY, *Chief Judge*, MAJOR and SWAIM, *Circuit Judges*.

SWAIM, *Circuit Judge*. The petitioner, Julian Lentin, seeks a review of the decision of the Tax Court of the United States which held that petitioner was not entitled to the deduction of $34,985.94 which petitioner claimed in his income tax report for the year 1946 as an "ordinary and necessary" expense incurred in carrying on his business during that year.

The amount claimed was paid by the petitioner to satisfy his part of a judgment which was rendered against him in the United States District Court for the Northern District of Illinois, Eastern Division, in a civil action brought against him and another by the Price Administrator for having "knowingly and willfully" sold lumber at prices in excess of the maximum prices established pursuant to the Emergency Price Control Act of 1942, as amended, 56 Stat. 23, 50 U. S. C. A. App. § 925(e). The District Court in that action expressly found that the overcharges had been made knowingly and willfully and therefore fixed the amount of the judgment at twice the

amount of the overcharges, as permitted by the Act only where the overcharges had been willfully made.

Prior to a hearing before the Tax Court, held in Chicago November 30, 1953, the parties stipulated that the entire record in the OPA case should be considered in evidence in the tax case. This stipulation recited the facts as to the District Court action against petitioner and showed that the District Court expressly found that when such sales were made Lentin knew that they were over the maximum prices fixed by the OPA and that the sales were in violation of OPA regulations. By this stipulation the parties agreed that either party might introduce further evidence, but in the November 30, 1953, hearing before the Tax Court the parties presented no further evidence and agreed that the case had been fully "stipulated."

The Tax Court sustained the Commissioner of Internal Revenue in his denial of the petitioner's claim of a deduction for the amount of the judgment which the petitioner had paid. The Tax Court recognized that the principal issue before it was whether or not the petitioner's violations of the Price Control Act were willful, and held that it was not necessary for it to redetermine the question since "the District Court's decision, affirmed on appeal, is *red judicata*, as to the issue of petitioner's willful violation of the Price Control Act."

The petitioner here contends that the Tax Court committed error: (1) in holding that the determination of the District Court, that petitioner's violations of the Price Control Act were willful, was *res judicata* as to the issue of willfulness in the proceeding in the Tax Court; (2) in refusing to allow that amount of the judgment representing the overcharge as a proper deduction; and (3) in refusing to allow an amount of the judgment equal to cost of goods sold as a proper deduction.

We think that the Tax Court in this case properly applied the doctrine of collateral estoppel in determining the question of whether the petitioner had willfully charged overceiling prices in violation of the Price Control Act. There was before the Tax Court in this case the entire

record of the action against the petitioner in the District Court, including all of the evidence and the express finding of the District Court that Lentin willfully and knowingly made sales at prices in excess of the maximum prices permitted by OPA regulations. This record also included the judgment for twice the amount of the overcharges, which amount was authorized only upon the court's finding of willful and knowing violations by the petitioner.

The petitioner contends that neither the doctrine of *res judicata* nor of collateral estoppel could have been properly applied by the Tax Court in the instant case.

The distinction between *res judicata* and collateral estoppel was pointed out and discussed by the Supreme Court in *Cromwell* v. *County of Sac.* 94 U. S. 351. The Court there, after explaining the doctrine of *res judicata,* said, at page 353, as to collateral estoppel: "But where the second action between the same parties is upon a different claim or demand, the judgment in the prior action operates as an estoppel only as to those matters in issue or points controverted, upon the determination of which the finding or verdict was rendered. In all cases, therefore, where it is sought to apply the estoppel of a judgment rendered upon one cause of action to matters arising in a suit upon a different cause of action, the inquiry must always be as to the point or question actually litigated and determined in the original action, not what might have been thus litigated and determined. Only upon such matters is the judgment conclusive in another action."

The courts have consistently recognized and applied the doctrine of collateral estoppel. *Commissioner of Internal Revenue* v. *Sunnen,* 333 U. S. 591, 595; *Lawlor* v. *National Screen Service,* 349 U. S. 322, 327; *Lynch* v. *Commissioner,* 7 Cir., 216 F. 2d 574, 579.

In *Lynch* v. *Commissioner of Internal Revenue, supra,* this court discussed and applied the doctrine of collateral estoppel as that doctrine was explained in *Commissioner* v. *Sunnen, supra.* The most recent decision concerning the doctrine of collateral estoppel which has come to our

attention is *Lawlor* v. *National Screen Service, supra,* which was announced by the Supreme Court June 6, 1955. In that decision the Court again recognized that the doctrine of *res judicata* applies where there is an attempt to retry the same cause of action, while collateral estoppel applies where the cause of action is not the same but there is an attempt to relitigate an issue which has theretofore been litigated between the same parties.

The petitioner insists that all of the cases cited by the Government on collateral estoppel involved two actions before the Tax Court and are therefore inapplicable in the instant case because here the first action was before the District Court. We have found no case which so limits the applicability of the doctrine of collateral estoppel, and we can think of no reason why such doctrine should be so limited.

The petitioner also contends that the nature of the Tax Court, as shown by the 1924 Act which created its predecessor, the Board of Tax Appeals, and designated it as an independent agency in the executive branch of the Government, precludes the Tax Court from determining facts on the doctrine of *res judicata* or collateral estoppel. The petitioner says that in that original Act the Board of Tax Appeals was designated as an independent agency in the executive branch of the Government; that this designation has been continued in subsequent laws; and that the Board of Tax Appeals and the Tax Court were given as their primary function the finding of facts in tax disputes. The petitioner admits, however, that the function of the Tax Court is of "an inherently judicial nature." Counsel for petitioner admits that he has found no decisions which expressly say that the Tax Court may not determine the facts in a case by the use of the doctrines of *res judicata* or collateral estoppel. Nor do we know of any reason why the Tax Court should relitigate the same action or the same issues which have theretofore been litigated before it or before any other court of competent jurisdiction by the same parties or by parties in privity with the original parties.

The petitioner in the instant case, to sustain his argument that the Tax Court was not permitted to resort to the doctrine of collateral estoppel to support its finding that he had willfully violated OPA regulations, also quotes the following language from the opinion in *Commissioner of Internal Revenue* v. *Heininger*, 320 U. S. 467, 475: "We hold therefore that the Board of Tax Appeals was not required to regard the administrative finding of guilt under 39 U.S.C. §§ 259 and 732 as a rigid criterion of the deductibility of respondent's litigation expenses." In that case, however, there was an administrative hearing held before the Solicitor of the Post Office Department and, there being some evidence which to the satisfaction of the Postmaster General indicated fraud, he issued fraud orders. Such an investigation and hearing are a far cry from the trial of the petitioner in the instant case in the United States District Court, a trial which resulted in a judgment that petitioner was guilty of willful violations of the Price Control Act.

There can be no real question as to the privity between the Price Administrator, who filed the action against the petitioner for violation of the Emergency Price Control Act, and the Commissioner of Internal Revenue, who disallowed the deduction claimed by the petitioner. As said by the Court in *Sunshine Coal Co.* v. *Adkins*, 310 U. S. 381, 402-3: "There is privity between officers of the same government so that a judgment in a suit between a party and a representative of the United States is *res judicata* in relitigation of the same issue between that party and another officer of the government." See also *United States* v. *Willard Tablet Co.*, 7 Cir., 141 F. 2d 141, 143.

The petitioner in this case relies strongly on certain language used by the court in *Jerry Rossman Corp.* v. *Commissioner of Internal Revenue*, 2 Cir., 175 F. 2d 711, as supporting his contention that the Tax Court had the duty of independent judgment on the issue of whether or not the claimed deduction would frustrate public policy. In that case the court stated that some penalties are deductible and some are not, and that in each case the court must decide *ad hoc* the question as to the deterrent effect

of exacting the penalty and whether failure to exact such a penalty would frustrate the policy of the particular act.

In the *Rossman* case the petitioner was clearly not guilty of any willful violation of the OPA regulations. The petitioner there became aware that he had violated the applicable regulations issued by the Office of Price Administration. Before that Office had started any investigation concerning his business, the president of the petitioner, on learning of the violation, sought the advice of the OPA as to what his company should do, and was advised that the company should return the overcharges to its customers. That being impractical because of the large number of customers involved and because the petitioner's customers had passed the overcharges on to those to whom they had sold, it was decided and agreed that the payment of the gross amount of the overcharges should be to the United States. Since the taxpayer there was clearly not guilty of willful violation of OPA regulations, the refusal to allow a deduction of the amount paid to the Government for the overcharges would not deter others from willfully violating the Act, nor would the allowance of the deduction encourage others to willfully violate the Act. The court there properly held that the amount paid by the petitioner should have been allowed as a tax deduction.

In the instant case, however, the Tax Court, by the agreement of the parties, had before it for its consideration as evidence the entire record in the OPA case. In its opinion the Tax Court recited the finding of the District Court that sales of lumber by the petitioner "were knowingly and willfully made by him and were known by him at the time to be in violation of the applicable regulations." The Tax Court then stated that where payments were made by a taxpayer pursuant to judicial determination that the taxpayer had been guilty of willful violations of the Emergency Price Control Act, such payments were not deductible from the taxpayer's gross income; that the disallowance of such deductions was "grounded on the principle that their allowance would frustrate clearly defined public policy." The Tax Court cited several authori-

ties as sustaining this holding. We think that under the facts before that court its decision on this point was correct. *National Brass Works, Inc.* v. *Commissioner of Internal Revenue,* 9 Cir., 205 F. 2d 104.

The petitioner next argues that he is at least entitled to a deduction for the actual amount of the overcharges. On this point the petitioner again relies on some of the statements made by Judge Hand in *Jerry Rossman Corp.* v. *Commissioner, supra.* But, as we pointed out above, Judge Hand was there dealing with violations of the OPA regulations which were innocently made by the taxpayer and, therefore, were not knowingly and willfully made as in the instant case. Here the evidence clearly showed, and the District Court so found, that the sales by the petitioner at prices in excess of the maximum prices "were knowingly and willfully made by him and were known by him at the time to be in violation of the applicable regulations." It therefore seems clear that under the facts here the entire amount which petitioner was required to pay in satisfaction of the District Court judgment must be considered, as the Tax Court held, a penalty which could not be mitigated by the allowance of a deduction without frustrating the policy of the Emergency Price Control Act.

The petitioner here argues at length that the doctrine of collateral estoppel cannot be applied where the burden of proof in two actions is on different parties. The petitioner says that in the OPA case he had the burden of proof to show that he was not guilty of willful violations of the OPA regulations, but that in the case before the Tax Court the burden of proof shifted to the Commissioner. We cannot agree that there was such a shift in the burden of proof. In the case before the Tax Court the petitioner was claiming a deduction and the burden was upon him to prove facts which would entitle him to the deduction. *National Brass Works, Inc.* v. *Commissioner of Internal Revenue,* 9 Cir., 182 F. 2d 526, 530; *George Schaefer & Sons* v. *Commissioner,* 2 Cir., 209 F. 2d 440. In the latter case the court said, page 442: "Accordingly, we think the taxpayer, absent proof of such innocence, cannot deduct the settlement payment as a business expense,

because to do so would be to frustrate the clear policy of the OPA statute."

Finally, the petitioner says that he actually realized a profit of less than $3,000.00 on the sales here in question, and that he is at least entitled to a deduction of $14,492.92 which he paid in excess of the ceiling price for the lumber in question—that this amount represents the cost of the goods sold. But the Tax Court properly held that since the petitioner had already included in his return as cost of goods sold the amount of $14,492.92(representing his share of the overceiling price paid for the lumber, there was no legal basis for permitting a second credit or deduction for that amount.

The decision of the Tax Court is

AFFIRMED.

A true Copy:

Teste:

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Clerk of the United States Court of Appeals for the Seventh Circuit.

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